TAX ALERT 2015-2

Efforts to Repeal Estate Tax Will Meet an Early Demise

OVERVIEW
With a federal estate tax exemption of $5,430,000 in 2015 (which increases each year by an inflation adjustment), approximately 99.8% of all estates are not subject to federal estate tax. However, that will not stop efforts to modify the tax. The President seeks to expand its scope by decreasing the estate exemption and curtailing some planning strategies. Republicans seek an outright repeal of the tax. Estate taxes were introduced sporadically to finance war efforts, including the Civil War, the Spanish-American War and World War I. The tax was made permanent following World War I. The rates have fluctuated over the years, hitting a high of 70%. The tax was even briefly repealed in 2010. Over the past few decades, the law remained in flux but with one consistent element: it was always highly controversial.

As a preliminary step towards repeal, on April 16, 2015, the House of Representatives passed a bill -- the Death Tax Repeal Act of 2015 -- by a vote of 240 to 179 that would repeal the estate and generation-skipping transfer taxes. Although the gift tax is preserved, the top rate would be reduced. A companion measure has been introduced in the Senate, but it is not known whether or when it will be brought to the Senate floor for a vote. The bill is generally supported by Republicans and opposed by Democrats; the President said he would veto it. Although there is no likelihood of this bill currently becoming law, it provides insight into the Republican and Democratic views on transfer taxes. It is also possible that it could be the subject of future legislation, especially depending on results of the 2016 elections.

ESTATE TAX REPEAL
The bill would repeal the estate tax, effective for decedents dying on or after the date of enactment. There also is a transition rule for a decedent dying before the date of repeal, for certain distributions to the surviving spouse from qualified domestic trusts (trusts created for non-citizen surviving spouses). In such a case, estate tax will not be imposed on (1) trust distributions made after 10 years from the date of repeal or (2) assets remaining in the qualified domestic trust upon the death of the surviving spouse.

GENERATION-SKIPPING TRANSFER TAX REPEAL
The bill would repeal the generation-skipping transfer tax, effective for generation-skipping transfers on or after the date of enactment.

MODIFICATIONS OF GIFT TAX
The bill would retain the gift tax but reduce the top rate from 40% to 35%, effective for gifts made after the date of enactment. The lifetime gift exemption would be the same as under current law - $5 million, adjusted for inflation after 2011 ($5,430,000 in 2015).

The bill would also reinstate section 2511(c) of the tax code, which would provide that a transfer to a non-grantor trust would be treated as a completed gift for gift tax purposes. This would effectively eliminate so-
called DING trusts (Delaware Incomplete Non-Grantor trusts), which may be used in certain states to save state income taxes. We have a separate Wealth Strategy Report on DING Trusts.

INCOME TAX BASIS
As confirmed in an accompanying Report of the Ways and Means Committee, the bill does not amend the rules for determining the income tax basis of assets acquired by gift or from a decedent. Accordingly, property received from a donor of a lifetime gift generally receives a carryover basis, and property acquired from a decedent’s estate generally receives a stepped-up basis.

REASONS FOR CHANGE
The Committee Report sets forth the reasons given by Republicans in support of the bill:

The Committee believes the Federal estate and generation-skipping transfer taxes harm taxpayers and the economy and therefore should be repealed. A tax on capital, such as the estate tax, motivates wealth holders to reduce savings and increase spending during life, rather than passing it to the next generation, ultimately increasing the consumption gap between the wealthy and poor...The Committee is particularly concerned about the effect of the estate tax on the owners of farms and family businesses, which create jobs and support our economy.

The Report also sets forth the dissenting views of Democrats:

The estate tax has been an important component of our tax code that promotes fairness and reduces economic inequality. Repeal of the estate tax would increase the deficit by more than a quarter of a trillion dollars to provide tax cuts to the wealthiest estates in our country. Estate taxes promote fairness by providing an essential counter-weight to the extraordinary benefits conferred on inherited wealth under our income tax system, and work to mitigate the impacts of wealth inequality.

CONCLUSION
The Death Tax Repeal Act of 2015 has been passed only by the House of Representatives. Even if passed by the Senate, it is certain that the President would veto it. However, the transfer tax proposals are worth following, especially due to the 2016 elections, which might alter the political landscape.

-National Wealth Planning Strategies Group

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